

# CPF limits and your mortgage

Do your sums to ensure you have enough CPF funds to service the loan in order to avoid forking out too much cash

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EVEN though it may seem like a good idea to maximise the repayment period on your home loan to reduce your monthly instalments, there are several risks you should be aware of before you do so.

One potential pitfall is that you might not be able to use your Central Provident Fund (CPF) savings to pay for your loan instalments during the last few years of the loan period.

Since 2003, any purchase of a Housing and Development Board (HDB) or private property with a bank loan will be subjected to a cap on the amount of CPF savings you can use to repay the loan.

The cap, known as the CPF Withdrawal Limit, is currently set at 132 per cent of your property's Valuation Limit. This will fall to 126 per cent next year and 120 per cent in 2008. The Valuation Limit is the lower of the property's valuation or purchase price.

But if you are living in an HDB flat, whether directly purchased from the board or from the resale market, and the flat is financed by a HDB concessionary rate loan, you are not subjected to the CPF Withdrawal Limit.

The CPF Withdrawal Limit means that homebuyers will likely have to service their bank loans entirely in cash some time in the later years of the 30-year loan tenor.

But that's not all.

Even before you reach the CPF Withdrawal Limit, another restriction kicks in when borrowers have used their CPF savings to pay 100 per cent of the Valuation Limit. After you reach 100 per cent of the Valuation Limit, you can continue using your CPF funds to pay for your housing loan instalments only if you have set aside the CPF Minimum Sum cash component in your Ordinary and Special Accounts.

In line with the Government's efforts to improve the adequacy of funds for retirement,



**BORROWER BEWARE:** Any purchase of a private property or HDB flat financed with a bank loan will be subjected to a cap on the amount of CPF savings you can use to repay the loan.

the CPF Minimum Sum was raised to \$94,600 on July 1 from \$90,000. The CPF Minimum Sum cash component equals half of that, or \$47,300. By year 2013, the CPF Minimum Sum is expected to increase to \$120,000 and the cash component would then be \$60,000.

"If you have not have met the Minimum Sum requirement ... you cannot continue using your CPF for housing loan instalments," said Mr Dennis Ng of mortgage consultancy Leverage Holdings.

This means that you have to start forking out your monthly instalments entirely in cash even before it reaches 132 per cent of the Valuation Limit. A homeowner who purchases a \$200,000 HDB flat and finances it with a 30-year bank loan with an average annual interest rate of 3.5 per cent may have to start forking out cash as early as the 20th year of the loan (See box).

"Hence, it might be prudent to get a 20-year loan instead, or set aside enough cash for the final years of the loan instalments," said Mr Ng.

Another important point for a homebuyer to note before committing to the maximum

loan tenor is the salary ceiling on CPF contributions.

For example, a person who is earning \$3,000 today would have \$660 contributed to his CPF Ordinary Account every month which can be used to pay for the monthly instalment on the housing loan.

But once he hits age 51, only \$360 would be contributed to his CPF Ordinary Account every month assuming that he earns the same in today's terms. This means he would have to top up \$300 for the difference in cash to pay for his housing loan instalment. This is provided that CPF contributions for each age band remain unchanged during his loan period.

"So if he took on a 30-year loan at age 30, he would be close to 60 years old before he finishes paying for the house. Between 51 to 55 years old, he may need to fork out more in cash," said Mr Ng.

Property agents usually do not share such potential problems with homebuyers because they are more interested in closing the deal. Thus, it falls upon the consumers to do their own calculations or seek help from loan consultants.

## HOME FINANCING CASE STUDY:

Mr Tan bought an HDB flat at a purchase price of \$200,000, a discount from its valuation of \$210,000.

As such, the Valuation Limit, which is the lower of the valuation and purchase price, is \$200,000.

He can use his CPF savings for the downpayment and instalments up to the valuation limit or \$200,000 without any restriction.

If he takes a 30-year bank loan of \$160,000 (80 per cent of purchase price) and assuming an annual average interest rate of 3.5 per cent, his monthly instalment works out to \$718.47.

As he has already used \$30,000 in his CPF account for the downpayment, he can use \$170,000 of his CPF to pay his monthly instalments given the Valuation Limit of \$200,000.

Using \$170,000 divided by the monthly instalment of \$718.47, he would reach his Valuation Limit in 236.6 months, or 19.7 years. This means that on the 237th month, if he does not have enough in his CPF to meet the CPF Minimum Sum cash component, he can no longer use his CPF funds to pay for the monthly instalments.

If Mr Tan took up a 30-year housing loan thinking he can use his CPF savings to pay for all the loan instalments, he might be in for a rude shock.

The last 123 months, or 10.3 years of his loan, may have to be paid for in cash.

What's more, if Mr Tan plans to buy a property financed by a bank loan from 2008 onwards, the CPF Withdrawal Limit would be reduced to 120 per cent or even lower, aggravating his problem.

## 'Amazing Bank Race' for kids

THE Hongkong and Shanghai Banking Corp (HSBC) has launched the "Amazing Bank Race", a financial education programme that promotes financial literacy and good money management habits among school children from ages 10 to 12.

Children participating in the race will be divided into teams of six, with each team given \$15 in game cash and \$20 in a 'checking account'.

Teams will have to complete tasks such as banking transac-

tions and budgeting their expenses.

The winning team is the one that completes all the challenges in the shortest time and has the most money left.

A total of seven sessions will be held on Saturdays from 9am to 12.45pm, from Aug 5 until Sept 30.

Participation is free and members of the public who are interested can register their children at [www.hsbc.com.sg](http://www.hsbc.com.sg) before July 31.

## WEALTH ANSWERS YOUR QUESTIONS

A NEW section to answer all your questions on personal finance and investment starts next weekend in Wealth. Called Financial Advisor, it will feature one question from a reader that will be answered by a relevant expert. So if you have ever wondered what a deductible is or why bond prices fall when interest rates rise, please send in your queries to [wealth@newstoday.com.sg](mailto:wealth@newstoday.com.sg) and you might just get your question answered.



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